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SIPDIS

DEPT FOR AF/S/KGAITHER; AF/EPS; EB/IFD/OMA
USDOC FOR 4510/ITA/MAC/AME/OA/DIEMOND
TREASURY FOR OAISA/BARBER/WALKER/JEWELL
USTR FOR COLEMAN
LONDON FOR GURNEY; PARIS FOR NEARY

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TAGS: ECON EINV EFIN ETRD BEXP KTDB PGOV SF
SUBJECT: SOUTH AFRICA ECONOMIC NEWSLETTER
July 22 2005 ISSUE

¶1. Summary. Each week, AmEmbassy Pretoria publishes an economic newsletter based on South African press reports. Comments and analysis do not necessarily reflect the opinion of the U.S. Government. Topics of this week's newsletter are:

- BER Predicts 4.2% Economic Growth;
- Weak Rand, Foreign Investors Lift JSE to Record High;
- Reserve Bank Seals $1.5 Billion Loan Deal;
- South African Airways Flights Cancelled as Strike Begins;
- Pepsi Returns to SA;
- SABMiller To Become World's Third-Largest Brewer;
- Mboweni Outlines Monetary Union Based on Rand and Pula;
- Top-level Talks on Life Insurance Rulings;
- ICASA Forces Telkom to Cut Charges;
- Manufacturing Production Declined Sharply in May;
- Real Building Plans Rose by 60.3% in May; and
- Cement Sales up 10.3% in First Half of 2005.

End Summary.

BER Predicts 4.2% Economic Growth

¶2. Low interest rates, strong domestic spending and a possible recovery in the export sector are likely to spur economic growth to 4.2% this year. Data released by the Bureau for Economic Research (BER) shows that gross domestic product (GDP) growth, which accelerated to 3.7% last year, is expected to rise in line with the government forecast of 4.3%. Bureau Chief Economist Pieter Laubscher warned, however, that an uncertain international environment, including terrorism, oil price volatility, and U.S. dollar and interest rate uncertainty clouded the outlook. Domestically, South Africa's current account deficit and currency volatility remain a concern. The current deficit stood at 3.8% of GDP in the first quarter of this year. BER sees the economy growing at 3.9% next year, but a sharper than expected increase in domestic interest rates and weaker global economic growth could produce a more pronounced domestic economic slowdown in 2006. BER forecasts that while the rand may strengthen to R6.50 to the dollar, the rand is likely to weaken to R7.50 next year due to weaker commodity prices, higher international interest rates, and a wider current account deficit in South Africa. Source: Business Day, July 22.

Weak Rand, Foreign Investors Lift JSE to Record High

¶3. The JSE Securities Exchange raced to another record high, buoyed by a weaker rand and increased demand from foreign investors. The all-share index topped out at 14,820.24 on July 14 before closing at 14,779.75. Rumors that Citigroup was interested in acquiring FirstRand's local bank, First National Bank (FNB), also helped propel the local bourse higher. When the rumor broke out on July 12, FirstRand's stock gained 5.8% to R15.05 before closing at R14.90. FirstRand's CEO Laurie Dippenaar confirmed there had been talks with Citigroup as well as HSBC and Standard Chartered. Analysts said they were optimistic about the prospects for the JSE, which has gained 16% in the year to date, and said equities remained the favored asset class in the long term. Economist Colen Garrow said that foreign buying accounted for almost R30 billion ($4.6 billion) so far this year. Last year, foreigners bought R38 billion ($5.8 billion) in JSE listed shares. Source: Business Day, July 15.

Reserve Bank Seals $1.5 Billion Loan Deal

¶4. The South African Reserve Bank has concluded a $1.5 billion dual-term loan which allows it to repay existing debt at lower interest cost. According to Reserve Bank Governor Tito Mboweni, SARB's loan was oversubscribed and drew participation from more than 30 banks across the globe. Tranche A is $1 billion with a three-year maturity and a margin of 22.5 basis points over LIBOR (the London Inter-Bank Offered Rate). Tranche B is for $0.5 billion with a five-year maturity and a margin of 30 basis points over

LIBOR. "South Africa's attractiveness as a borrower is reflected by the Moody's ratings upgrade in January this year," said Mboweni. Rating agency Moody's upgraded South Africa's credit rating from Baa2 to Baa1 with a stable outlook, primarily based on the "strengthening" in the country's foreign reserves position. The 24 mandated lead arrangers (including Deutsche Bank, JP Morgan, and Citigroup) initially committed $62.5 million each, but later scaled back their commitment to $56 million. Source: Business Day, July 19.

South African Airways Flights Cancelled as Strike Begins
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¶5. All South African Airways (SAA) flights leaving from Johannesburg and Cape Town International Airports were grounded Friday morning (July 22) as the airline's employees embarked on a nationwide strike. Extremely long queues formed at the domestic departures section of the Johannesburg International Airport as a strike by ground staff and cabin crew kicked off. Apologetic SAA managers were walking up and down the queue explaining that the strike was causing "chaos." Police were on standby, close to the queues, but were not expecting any serious problems. No crowds had gathered to picket at the airport. United Association of South Africa (Uasa) said thousands of its members would take part in the strike following a deadlock in pay negotiations. Uasa is the largest representative union of ground staff and cabin crew at SAA. It was not yet clear whether members of fellow trade union, the South Africa Transport and Allied Workers Union (SATAWU), were also on strike. Both unions demand an 8% increase while SAA is offering 5%. Source: Business Day, July 22.

Pepsi Returns to SA

¶6. A South African cola war is on the verge of breaking out again with PepsiCo International's decision to enter the local market for a third time. PepsiCo tried to return in the 1990s, but, its partner, black empowerment company New Age Beverages, went bankrupt owing PepsiCo $100 million. On July 20, PepsiCo signed an agreement with beverage giant Pioneer Foods that should result in Pepsi products finding their way onto retail store shelves by December. Under the agreement, the Pioneer beverage subsidiary, Ceres Fruit Juices, will bottle and distribute the PepsiCo soft-drinks, including Pepsi, Diet Pepsi, 7-Up, and Mirinda. Pioneer produces more than 60 South African household foods and beverage brands. Rival Coca-Cola supplied the South African market through Swaziland during apartheid and has secured an 80% market share. Source: Business Day, July 21.

SABMiller To Become World's Third-Largest Brewer
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¶7. The owners of South America's No. 2 brewer, Bavaria SA, agreed to a $7.8 billion stock swap and cash deal with SABMiller that will create the third-largest brewer in the world by volume and profit, behind InBev and Anheuser Busch. SABMiller said it was buying a 71.8% stake in Colombia-based Bavaria from the Santo Domingo family by issuing 225 million shares worth about $3.5 billion. SABMiller will also pay about $2 billion in cash and take on Bavaria's debt of $2 billion. After the announcement, SABMiller shares, which had fallen in anticipation of a costly deal, were up 10.6% in London. In Johannesburg, the stock was up 10.2% at a new high of R114.5. SABMiller, which brews Miller, Castle, and Peroni beers, said the combined group would have annual beer volumes of about 175 million hectolitres and proforma aggregated net revenues of about $12.5 billion. Source: Business Day, July 19.

Mboweni Outlines Monetary Union Based on Rand and Pula
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¶8. On July 12, Reserve Bank Governor Tito Mboweni floated plans for a monetary union among the members of the Southern African Development Community (SADC) that would be based on the South African rand and the Botswana pula. The 13-member SADC bloc has agreed to create a common currency and a regional central bank by 2016. African Harvest Fund Managers Chief Economist Adenaan Hardien said such a monetary union would require a common interest rate and harmonized fiscal policies, which could be problematic -- "as some of the European Union countries are finding out." Furthermore, SADC economies were at different stages of development, so a one-size-fits-all monetary policy could present problems, Hardien said. Mboweni argued that it would make sense for the common monetary area of South Africa, Lesotho, Swaziland and Namibia to form the basis of a regional central bank, which could then invite other SADC member states to join. The SADC consists of South Africa, Angola, Botswana, the Democratic Republic of Congo, Lesotho, Malawi, Mauritius, Mozambique, Namibia, Swaziland, Tanzania, Zambia and Zimbabwe. Source: Business Day, July 13.

Top-level Talks on Life Insurance Rulings

¶9. The Financial Services Board (FSB) and the Life Offices Association (LOA) held the first of a series of private meetings as tension mounted between life insurers and the pension funds adjudicator. Adjudicator Vuyani Ngalwana has issued a spate of rulings over the past three months, hammering the life insurance companies for poor disclosure of costs they levy on retirement annuities. No details have emerged as the meetings were deemed "private." Newly appointed FSB head Rob Barrow declined to comment on the outcome. This meeting came after the association, an industry body representing life insurers, called on the FSB as the regulator of the insurance sector to take urgent action to resolve the looming crisis in the industry. As the regulator governing the industry, the FSB regulates the capital adequacy requirements of life insurers, but it does not regulate product and costs. The life insurance companies have appealed against a number of Ngalwana's rulings, and the parties could decide on what steps to take only after the high court had given judgment. It is estimated that retirement annuities account for between 5% and 25% of a typical life insurer's liabilities -- making it an important leg of their business. Source: Business Day, July 19.

ICASA Forces Telkom to Cut Charges

¶10. The Independent Communications Authority of South Africa (ICASA) obtained government approval last week to cap Telkom's price increases at 3.5% below inflation. The new pricing cap is tougher than a previous price-rise limit of 1.5% below inflation. Telkom will cut the prices of some of its services to comply with a regulator ruling capping its overall rate of increase, spokesman Xolisa Vapi said. Vapi did not say, however, which services would see lower tariffs. Telkom's new prices, submitted to government in response to ICASA's ruling, are likely to be announced as early as July 25. Telkom has been criticized for charging too much for calls, Internet access, stalling the roll-out of phone lines and inflating the cost of doing business in South Africa. Deputy Communications Minister Roy Padayachie said at a meeting on telecommunications pricing that call costs were one of the main barriers to foreign direct investment and growth. Government has been chipping away at Telkom's monopoly with new laws that let value-added network operators offer cheaper calls over the Internet. However, the Department of Communications has been accused of dragging its feet over the launch of a second network operator and critics say Telkom continues to dominate the market and rip off customers. Telkom has slashed the cost of international calls in recent months, as well as prices for high-speed Internet access, but has offset this by increasing local call tariffs and rental and connection fees. Source: Business Day, July 18.

¶11. Comment: Based on a July 18 discussion document, ICASA is also set to probe high mobile phone charges. Competition between the three mobile network operators (Cell C, Vodacom, and MTN) has failed to bring their tariffs down to an acceptable level and the regulatory authority may impose a one-off reduction in the fees or introduce more stringent pricing policies. End Comment.

Manufacturing Production Declined Sharply in May
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¶12. Manufacturing output fell by 2.6% on a seasonally adjusted basis during May following strong growth in previous months. Production of furniture, food and beverages as well as clothing and textiles fell sharply by 8.7%, 6.0%, and 4.3%, respectively. Output of communication apparatus and wood and paper products increased by 14.2% and 0.4%, respectively. Overall output increased by only 1.7% in the three months ending in May compared with the previous three months on a seasonally adjusted basis. Future manufacturing output growth is expected to be relatively subdued off the high base established in 2004. Source: Nedbank, July 12.

Real Building Plans Rose by 60.3% in May

¶13. The real value of building plans passed in South Africa rose by 60.3% year-on-year (y/y) in May 2005 to a record R4.2 billion (all figures constant 2000 rand) compared with a 79.4% increase in April 2005 to R3.6 billion, Statistics South Africa reported. This brought the increase for the first five months to 47.6%, which is substantially higher than last year's upwardly revised 35.2% increase after only an 11.3% rise in 2003. The largest increase in 2004 in the value of recorded building plans passed was reported for residential buildings (up 41.3%), followed by additions and

alterations (up 29.0%) and non-residential buildings (up 23.4%). The 2004 peak increase of 77.6% was set in February. January 2004 was the only month last year, where the y/y increase did not exceed 20%, while there were four months when the y/y increase exceeded 45%. Source: I-Net Bridge, July 20.

Cement Sales up 10.3% in First Half of 2005

¶14. South African cement sales for the first half of 2005 rose by 10.3% year-on-year (y/y) to 5.5 million tons, the Cement and Concrete Institute (CNCI) reported. The increase in June was 6.9% y/y of 1.07 million tons after May's 8.1% y/y rise of 1.02 million tons after April's large 28% surge of 972,000 tons. Cement sales rose only 2.1% y/y in March 2005 to 925,000 tons. Cement sales rose by 17.4% in 2004 to a record 10.69 million tons compared with a 7.0% rise in ¶2003. Source: I-Net Bridge, July 20.

HARTLEY